Since July 1994, during the conduct of the above detailed dockets, the Department has endeavored to ensure that: (1) all telecommunications providers, new entrants as well as incumbent telephone companies, are able to fairly compete in the Connecticut telecommunications market; and (2) the interests of the Connecticut public are protected. To date, the efforts of the Connecticut legislature and the Department have resulted in the certification of 19 companies to offer retail local telecommunications services in Connecticut in direct competition with the incumbent telephone companies; six additional applications are pending before the Department.[2] Under terms and conditions set forth by the Department in Docket No. 94-07-03, every CLEC is committed to serving any customer in its Modified Local Market Area(s), i.e., any residential or business user that requests service, within three years of the CLEC's certification. The legislative goal that Connecticut residents be afforded a greater choice among telecommunications products, providers, and prices is being realized in the concerted efforts to date of this Department.

D. THE TELECOMMUNICATIONS ACT OF 1996

More than a year and a half after Connecticut opened its telecommunications markets to competition, the United States Congress enacted legislation, in the form of the Telecommunications Act of 1996 (1996 Federal Act), designed to revise national telecommunications policy and to remove unwarranted statutory and court-ordered barriers to competition among segments of the telecommunications industry. Upon review of the federal legislation the Department is of the opinion that the policies and positions adopted by the Department in response to Public Act 94-83 are generally in accord with provisions contained in the 1996 Federal Act.[3]

E. DOCKET SCOPE AND CONDUCT OF THE PROCEEDING

As evidenced in the discussion of the implementation dockets contained in subsection B of this section, the Department's relevant efforts to date have focused on: (1) providing greater access to the Connecticut telecommunications markets historically served by the state's three local exchange companies (LECs), The Southern New England Telephone Company, The New York Telephone Company and The Woodbury Telephone Company; (2) setting rules and prices for local exchange access by

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[2] Under terms and conditions set forth in Docket No. 94-07-03, the Department has to date approved applications for CLEC authority from AT&T, Brooks Fiber Communications of CT, Inc., Cablevision Lightpath of CT, Inc., Cable & Wireless, Inc., Commonwealth Long Distance Company, CRG International, CT Telephone & Communications Services, Dial & Save of Connecticut, Inc., Excel Communications, Inc., GE Capital Communications et al, Intermedia Communications, Inc., LCI International Telcom Corp., LDDS/WorldCom, MCI Metro, MFS Intellenet, Sprint, TCI Telephony of CT, Inc., Teleport Communications Group, and WinStar Wireless of CT.

[3] One discrepancy between federal and Department policy is in the pricing of wholesale local basic service. See Decision, Docket No. 96-03-19, Petition of The Southern New England Telephone Company for Suspension of Section 251(c)(4) of the Telecommunications Act of 1996, May 17, 1996. Additionally, in its Decision in Docket No. 94-07-05, the Department limited the offering of customer owned coin telephone (COCOT) service in Connecticut to LECs and CLECs. However, the Department recently re-opened Docket No. 94-07-05 to reexamine the terms and conditions under which COCOT service will be offered in Connecticut.

competitors to those portions of the incumbent LECs' infrastructures necessary to the development of competition; and (3) reducing the level of Department involvement deemed necessary in matters of competitive conduct.

In the instant docket, however, the Department sought to critically examine the financial, structural and operational impact on SNET of broader competition and increased discretionary authority resulting from the Department's previous implementation efforts, the development of competition and introduction of the 1996 Federal Act Specifically, the Department is compelled to examine the constructs and the conduct of SNET and its subsidiaries to ensure that affiliate strategies, operational structures and performance standards conform with the prevailing rules and regulations governing telecommunications providers. Therefore, on December 6, 1996, the Department issued a Statement of Scope of the Proceeding in this docket expressing its intention to examine the following:

- the organizational and operational structures proposed by SNET to pursue the roles and responsibilities accorded it by Public Act 94-83, the 1996 Federal Act and prior Department decisions;
- the legal/regulatory provisions, technological considerations and market conditions that serve as planning limitations on SNET in the proposed organizational and operational structures;
- the scope and scale of the financial transactions envisioned by SNET's proposed organizational and operational structures;
- whether there exists a uniform set of managerial principles governing the formation, operation, evaluation and dissolution of affiliate business relationships;
- the basis for determining cost and/or assigning value to any relationship with, or offering by, one affiliate business unit to another;
- the scope of independent operational authority and accountability accorded to managing officers of the respective affiliate business units; and
- the impact of any proposed organizational structure and/or affiliate relationship on the development of full and fair competition in Connecticut.

In order to efficiently accomplish that which the Department envisioned from this docket, the Department established a scope of directed inquiry involving a three-step development process (SNET submittal, comments by participants and reply comments by SNET). Initially, the Department directed SNET to file a proposed organizational and operational structure to be employed in Connecticut as its initial submission. SNET was also directed to include in its submission:

- the rationale for its organizational and operational structures sufficient to permit the Department to fully evaluate the relative merits of SNET's proposal;
- a description of the charter of each of the respective affiliate business units and their respective role within the SNET strategy, including products/services responsibilities where appropriate;
- a description of the scope of any service performed by an identified business unit or between business units and the corporate parent for 1997;
- a justification for having any such service performed by the identified business unit

or the corporate parent for 1997;

- a pro forma projection of the estimated monetary value of any such service performed in 1997 on behalf of an identified business unit by another business unit or the corporate parent, including a projection of the estimated monetary value if such service were to be performed within the identified business unit;
- a description of the scope of any common corporate services provided to the affiliate business unit by the corporate parent in 1997;
- a pro forma projection of the level of common corporate cost assigned to any identified business unit for 1997 as well as the allocation factor used to make such assignment; and
- a pro forma projection of the level of common corporate cost not assigned to any identified business unit for 1997.

Following SNET's filing, parties and intervenors were afforded opportunity to submit formal comments concerning relative risks and/or merits of SNET's submission.[4] SNET was subsequently afforded the opportunity to submit its reply to the comments of the other parties.

By Notice of Hearing dated February 3, 1997, public hearings were conducted on March 31, 1997 and April 1, 2, and 3, 1997 in the offices of the Department, Ten Franklin Square, New Britain, Connecticut 06051. The hearing was continued to April 17, 1997, at which time it was closed. The Department issued a draft Decision in this proceeding on June 5, 1997. Pursuant to Notice, all parties and intervenors were provided opportunity to file written exceptions and to present oral arguments on the draft Decision.

IV. SNET REORGANIZATION PROPOSAL

On January 1, 1997, SNET and the Telco (jointly, the Company) filed with the Department a joint proposal for reorganization of certain corporate operations. The major components of the reorganization proposal are as follows:

- SNET will separate the retail and wholesale business units that currently reside in the Telco.
- Upon the proposed effective date of the reorganization, January 1, 1998, the Telco will transfer all of its retail operations and retail customers to SNET America, Inc. (SAI),[5] and the Telco will no longer offer retail telecommunications services.
- SAI will offer to all end users a variety of retail services on a statewide basis, including local, intrastate, interstate, international calling, and a number of enhanced services.[6]

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[4] OCC and AT&T submitted comments regarding the SNET/Telco submission.

[5] SAI is a wholly owned subsidiary of SNET currently offering interstate and international long distance services in Connecticut..

[6] On March 18, 1997, SAI filed with the Department an application for a Certificate of Public Convenience and Necessity (CPCN) to become a certified local exchange carrier (CLEC). That application is being considered by the Department in Docket No. 97-03-17, Application of SNET America, Inc. for a Certificate of Public Convenience and Necessity

- SAI will be subject to the same state and federal regulatory requirements as are imposed on other CLECs.
- The Telco will continue to operate as a telephone company/public service company for purposes of Connecticut law.
- The Telco will restrict its business purpose to serving the needs of CLECs and other wholesale companies.
- The Telco will retain ownership and operational control of all distribution plant and core network infrastructure, and will be subject to all relevant state and federal requirements.
- The Telco will be regulated pursuant to the alternative regulation plan approved by the Department in the March 13, 1996 Decision in Docket No. 95-03-01, and will be regulated as an ILEC under federal law.
- The Telco will establish wholesale service tariffs for all existing Telco service offerings, priced initially at retail minus avoided cost, consistent with current federal pricing standards.
- The Telco will price new wholesale services at Total Service Long Run Incremental Cost (TSLRIC) plus a reasonable contribution to the Telco's overhead costs.
- The Telco will preserve tariffs for intrastate and interstate access and unbundled network elements as previously approved by the Department.
- The Telco's relationship with its affiliates will continue to be governed by Parts 32 and 64 of the FCC's regulations as embodied in the Telco's Cost Allocation Manual (CAM).

SNET's arguments supporting its proposal are detailed in the next section.

V. PARTICIPANTS' POSITIONS

A. THE SOUTHERN NEW ENGLAND TELECOMMUNICATIONS CORPORATION/THE SOUTHERN NEW ENGLAND TELEPHONE COMPANY

1. General Rationale in Support of Proposed Reorganization

The Company asserts that its proposed reorganization will focus the Telco on an aggressive wholesale strategy with a primary goal of encouraging and stimulating usage of the Telco's network by all service providers, thereby promoting local service competition. At the same time, SAI will be in a position to compete aggressively in the retail market further accelerating the benefits of competition in the retail market. According to SNET, the proposed reorganization will benefit CLECs, residents and businesses throughout the state.

The Company argues that reorganization is a necessary and logical response to the dramatic legislative changes of the last two years which have profoundly affected the telecommunications industry. Specifically, SNET contends that the passage of the 1996 Federal Act, and the FCC Order interpreting and expanding the reach of that act,[7]

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[7] First Report and Order, Implementation of the Local Competition Provisions of the Telecommunications Act of 1996 (FCC Order), August 8, 1996.

have compelled not only it but all industry participants to seriously reconsider their business strategies. From SNET's perspective, requirements in the 1996 Federal Act and the FCC Order coupled with the various state requirements have placed the Telco, as currently structured, in an untenable market position.

The Company contends that the most notable market disadvantage presented to the Telco is the requirement that it provide, at wholesale, essentially all of its retail telecommunications services including discount plans, service packages and promotions, at a 17.8% discount,[8] regardless of whether that discount brings the wholesale price below cost, a disadvantage that is exacerbated by a service-by-service imputation standard. According to the Company, the downward spiral created by the requirement that retail services be offered net of the wholesale discount essentially prevents the Telco from effectively competing with the CLECs, denies it the ability to differentiate its retail services from those of its competitors, and rules out any opportunity for the Telco to competitively price its retail services.

The Company argues that in contrast to the restrictive treatment of ILECs, the FCC Order secures the competitive viability of CLECs. In SNET's view, CLECs can readily differentiate their products by combining their own facilities with resold telco services creating new service packages, and changing their prices through discounts and promotions (as dictated by market conditions) without offering these discounts to other competitors. Moreover, the Company contends that given the resale requirements imposed on ILECs, CLECs are assured by law a competitive edge over ILECs in both pricing and product innovation.

Further, the Company argues that the Telco, unlike its competitors, is constrained by additional administrative burdens, including involved regulatory processes and cost study requirements, that deter the Telco's ability to both react quickly to the marketplace and maintain any long-term sustainable advantage effectively restricting the benefits of competition for the public.

The Company thus submits its proposed reorganization is the best available strategy to enable both the Telco and SAI to emerge as viable competitors in their respective markets. SAI will offer new and innovative services and bundles of services while the Telco will be a wholesale provider and offer fully functional telecommunications services and unbundled network elements to SAI and all other CLECs in a nondiscriminatory manner. In the Company's view, its proposed reorganization will promote the pro-competitive goals of the Act and the 1996 Federal Act, encourage competition and technological innovation in the marketplace. Company Brief, pp. 1-5, 10-14.

2. Public Act 94-83

SNET asserts that the focus of Public Act 94-83 is two-fold: the effective and efficient development of competition and protection of the public interest. The

[8] Except as otherwise provided in Interconnection Agreements.

Company contends that the proposed reorganization is consistent with these objectives. Specifically, in SNET's view, the proposed reorganization will promote wholesale competition by strengthening the Telco's ability to be an aggressive wholesale provider. Further, SNET asserts that reorganization will enhance retail competition by permitting SAI to fully participate in the retail market. The Company states that SAI's viability in Connecticut's competitive telecommunications marketplace will be defined by its ability to successfully bundle its available services. SNET envisions SAI answering competitors' offerings with a variety of telecommunications services, including local, intrastate, interstate, international calling, and a number of enhanced services to all end users. According to the Company, SAI's entrance into the market on equal footing with other CLECs will encourage competitive prices, increased choice for consumers, and innovative and expanded service offerings.

The Company next points to Public Act 94-83's goal to "utilize forms of regulation commensurate with the level of competition in the relevant telecommunications service market." Under the Company's proposal, upon the effective date of the reorganization, SAI will be regulated like all other CLECs while the Telco will continue to be subject to the rate regulation requirements previously adopted by the Department in Docket No. 95-03-01. In SNET's view, the continuance of the current regulatory structure is consistent with the Public Act. SNET Brief, pp. 23-27.

The Company further offers discussion regarding its proposed reorganization in the context of other Public Act 94-83 provisions. According to the Company, because SAI will be offering retail telecommunications services pursuant to its certification under Conn. Gen. Stat. § 16-247g, it will not be required to seek reclassification of its services from "noncompetitive" to "competitive" as would be required of the Telco by Section 16-247f of the Act. Furthermore, as a competitive telecommunications carrier, SAI will not (according to the Company) be subject to the imputation standard set forth in Conn. Gen. Stat. § 16-247b(b) for the Telco, but its retail tariff filings will be subject to Department review and approval just as are the retail tariff filings of other CLECs. The Company further explains that upon approval of SAI's request for a CPCN, SAI will be subject to those obligations set forth in the Public Act and in the Department's Decisions in Docket No. 94-07-03 and Docket No. 94-07-07 for all CLECs (e.g., the provision of service on a statewide basis within three years from certification, compliance with the post-certification filing requirements established by the Department, and the provision of "one local service offering that is equivalent in design and calling provisions to the basic, flat rate local calling package offered by the relevant telephone company").[9]

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[9] The Company further states that as a CLEC, SAI will be subject to certain market responsibilities contained in the 1996 Federal Act, including the requirement that SAI interconnect with other telecommunications carriers and allow resale of its services without unreasonable conditions or restrictions. SAI will also be required to provide: number portability to the extent technically feasible; dialing parity which includes nondiscriminatory access to telephone numbers, operator services, directory assistance, directory listings, with no unreasonable dialing delays; access to rights-of-way by competing providers at nondiscriminatory rates, terms, and conditions; and reciprocal compensation arrangements.

The Company states that following adoption of the proposed reorganization, the Telco, as a wholesaler, will continue to be broadly regulated by the Department. According to the Company, on the effective date of the reorganization, all existing retail offerings will be available to CLECs as wholesale services at prices equivalent to the price of the current comparable retail offering minus avoided costs; any new wholesale services and unbundled elements introduced after the effective date of the reorganization will be priced at their respective TSLRIC plus a contribution to joint and common costs. The Company states that any change in wholesale price will remain subject to the Department's approval. Once a new wholesale price is approved by the Department that wholesale service offering would then be subject to the Alternative Regulation Plan approved in Docket No. 95-03-01.

The Company asserts that with adoption of this proposal, the Telco will no longer be subject to the wholesale pricing standard set forth in §252(d)(B) of the 1996 Federal Act because the Telco will no longer be offering retail telecommunications services. Furthermore, the Company asserts that with adoption of this proposal SAI will not be subject to the imputation standard required of the Telco in Conn. Gen. Stat. §16-247b(b). However, the Company contends that the intent of both standards will nonetheless be preserved in the proposed reorganization. The Company maintains that under the proposed reorganization, SAI and the other CLECs will pay either tariffed rates or rates subject to publicly available interconnection agreements that must by law be nondiscriminatory and approved by the Department. According to the Company, this will level the playing field without regard for any inaccuracies inherent in the measurement of avoided costs or the difficulties associated with calculating the imputation standard thus fully achieving the purposes of the state standards as well as the federal standards.

The Company also maintains that the proposed reorganization will further the infrastructure development goals set forth in PA 94-83. According to the Company, just as SAI will be encouraged to innovate the wholesale company will be encouraged to innovate and invest. Specifically, with a major customer as its own retail arm and no longer "captive," the Telco will have to be competitive in pricing and product innovation in order to succeed.

The Company contends that the proposed reorganization will permit the Telco to focus on maintaining and investing in its network facilities and product development in order to serve and grow its wholesale customer base. In the Company's view, the Telco's goal will be to attract more competitors into Connecticut and onto its network through aggressive pricing and product development. The Company claims that benefits from the Telco's improved provisioning of wholesale services to CLECs will flow directly to their retail customers, which is consistent with the Public Act's goals that focus on network infrastructure sharing and development.

In addition, the Company asserts that with approval of the proposed reorganization, the Telco will continue to improve its capability and capacity for processing CLECs' orders as electronic interfaces continue to evolve. The Company notes that the Telco is currently in the process of completing the first development phase of its Mechanized Service Access Platform (MSAP) which will process information exchanges and wholesale service requests to and from the Telco and their CLEC customers. By January 1, 1998, the Telco will also have in place service measurements, service standards, and financial remedies for wholesale services and unbundled network elements.

In sum, the Company claims that the proposed reorganization will stimulate both wholesale and retail competition in the marketplace and ensure continued investment in and advancement of Connecticut's telecommunications infrastructure consistent with the expressed goals of Public Act 94-83. The Company states that increased competitiveness of the telecommunications marketplace warrants a regulatory framework commensurate with the level of competition, and commits the Telco to meeting its obligations as an ILEC even as it positions itself to be an aggressive wholesaler. Company Brief, pp. 27-33; Company Reply Brief pp. 2-28

3. The 1996 Federal Act and Successor Obligations

The Company states that its proposed reorganization will accelerate realization of the goals of the 1996 Federal Act. Specifically, the proposed reorganization will provide CLECs with nondiscriminatory access to the Telco's network facilities and encourage competition and innovation in the marketplace. A separate wholesale entity will also provide the necessary incentive and motivation for the Telco to meet and exceed the ILEC requirement to serve all CLECs and other telecommunications carriers in a nondiscriminatory manner and develop innovative services and technologies for these customers set forth in §251(c) of the 1996 Federal Act.

The Company argues that with approval of the proposed reorganization and the realignment of retail market responsibilities between the Telco and SAI, SAI will not by virtue of that realignment be an ILEC or be subject to ILEC obligations set forth for the incumbent local exchange carrier in §251(c) of the 1996 Federal Act. According to the Company, SAI is not currently, nor will it be in the future, an incumbent local exchange carrier (ILEC) as defined in §251(h)(1) of the 1996 Federal Act because it did not offer local exchange service in any area on the effective date of that act and will not be a "successor or assign" of the Telco on the effective date of the reorganization.

The Company is of the opinion that a critical factor dictating successor obligations is the underlying nature of the assets retained by the Telco. The Company maintains that if an entity succeeds to all of the assets of an ILEC then that entity is arguably a "successor or assign" of an ILEC and should be regulated as such. The Company contends, however, that should an entity receive only a limited portion of an ILEC's assets, and those assets are unnecessary to satisfy the ILEC's obligations under the 1996 Federal Act, then that entity does not become an ILEC by virtue of the transaction. Accordingly, the Company asserts that the nature of the assets transferred from an ILEC should be analyzed, in conjunction with its obligations under §251(c) of the 1996 Federal Act, to determine whether the transferee is truly a "successor or assign" of an ILEC and should succeed to the obligations of the ILEC.

The Company explains that following the proposed reorganization, all retail functions previously performed by the Telco will be the sole responsibility of SAI. All network facilities and personnel necessary to operate and maintain those facilities will remain in the Telco to enable the Telco to meet the full requirements of the 1996 Federal Act. Following the reorganization, the Telco maintains that it will continue to provide to all CLECs, including SAI, nondiscriminatory access to its network facilities and services just as now. Consequently, under the proposed reorganization, SAI will not own network, or control access to the Telco network facilities and therefore, will not have the ability to satisfy the ILEC duties as imposed by §251(c) of the 1996 Federal Act. The Company, therefore, concludes that there is no justification for finding that SAI will be a "successor or assign" of the Telco following the proposed reorganization.

Additionally, the Company cites a recent FCC order as guidance on the interpretation of the "successor or assign" provision of the 1996 Federal Act as well as the FCC's view toward the status of ILEC affiliates that offer local exchange services.[10] According to the Company, the FCC offered comment on these issues in an order concerning the relationships between the regulated business units of the Regional Bell Operating Companies (RBOCs) and the separate affiliates required of the RBOCs under 47 U.S.C. §272 to enter the interexchange services markets. Citing the FCC Order, the Company argues that since SNET will not be transferring ownership of any unbundled network elements to SAI, SAI should not be treated as an "assign" of the Telco. The Company also argues that the FCC has expressly confirmed that a BOC may establish a separate affiliate that will itself provide local exchange service, perhaps as a reseller of the BOC's bundled services or unbundled network elements. According to the Company, the FCC's touchstone in determining whether SAI should be subject to more extensive regulation as an ILEC is whether SAI controls "network elements" that should be made available to other CLECs. The Company argues that, because the Telco will control all required "network elements" and make them available on a nondiscriminatory basis to all requesting carriers (including SAI), it is improper to treat SAI as an ILEC. The Company thus concludes that, while the Telco will remain an ILEC under federal law and a telephone company/public service company under Connecticut law and will continue to satisfy all requirements imposed upon it by virtue of those classifications, SAI will be a CLEC and should be regulated as such.

While acknowledging that SAI may have a local service market share that is larger than other CLECs at the time of the reorganization, the Company asserts that this factor alone is not sufficient cause to construe SAI to be a "successor or assign" subject to ILEC obligations under the 1996 Federal Act. The Company argues that examining SAI's market power only in the retail local exchange market is improper and misleading. The Company claims that the relevant market in which SAI will compete following the proposed reorganization will be, at a minimum, the overall Connecticut telecommunications market including interstate services originating or terminating in

[10] First Report and Order and Further Notice of Proposed Rulemaking, CC Docket No. 96-149, Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act of 1934, as amended, FCC 96-489, released Dec. 24, 1996 ("Non-Accounting Safeguards Order").

Connecticut and will focus on the ability of competitors to offer packages of products and services. Because the market will consist primarily of bundles of telecommunications services, including local exchange service, the "relevant market" for determining SAI's market power following the proposed reorganization, should be the market of bundled telecommunications products. However, the Company states that even if the relevant market were deemed by the Department to be the Connecticut retail local exchange market, SAI will not have unfair market power because, as a result of Public Act 94-83 and the 1996 Federal Act, that market is now fully "contestable."

The Company further argues that while SAI will initially have a high share of the local exchange market, market share alone does not necessarily determine market power (i.e., the ability to control prices). The Company contends that the Public Act and the 1996 Federal Act have created a framework in which the Telco must resell all of its services and unbundle all of its network for market participants. Prices for Telco services must be available to all CLECs on the same terms and conditions. Moreover, SAI will be subject to all antitrust laws. Additionally, given the number of certified CLECs in the local exchange market, SAI will not be able to raise its prices without fear that other CLECs purchasing the same services from the Telco will undercut SAI's price. Therefore, SAI will not have market power to control prices following the reorganization.

The Company argues that reliance upon market share statistics in this instance is likely to be an inaccurate or misleading indicator of market power. The Company claims entry by prospective competitors into the Connecticut local exchange market is extremely easy. The Company further states that due to the 1996 Federal Act, all CLECs, including SAI, can purchase all Telco services for resale in the retail market. The Company contends that previous barriers to market entry, such as the prohibitive cost of constructing a network and facilities are no longer present. In the Company's view, CLECs can now compete in the local exchange market without a significant investment in either technology or personnel and it is for these reasons that the Company believes SAI's market share will not be sustainable over time.

Finally, the Company contends SAI's lack of market power will be further supported by the Telco's imminent loss of local exchange market share. The Company states that, while the Telco's customers will move to SAI on the effective date of the reorganization, the Telco expects significant market activity prior to that date. The Company expects a reduction in the Telco's market share for residential and business local service customers by January 1, 1998. The Company notes that the Telco has begun to experience local residential and business market share loss across the state, and expects by year end to lose even greater market share. Company Brief, pp. 34-49; Company Reply Brief, pp. 28-32.

4. Customer Marketing

The Company contends that some form of neutral customer education will afford customers opportunity to be better informed of their local carrier choices prior to the reorganization. While the Telco initially proposed bill inserts and public service announcements, the Company opposes any formal balloting process because of the inherent complexity and the potential for customer confusion. The Company further argues that balloting would be costly and is not necessary to make the local exchange market competitive. In support of its argument against balloting, the Company notes that when intrastate equal access was implemented, the Department found that customer balloting was not necessary. The Company points out that the market is now fully competitive, five months after the implementation of equal access. In the Company's view, there is no reason to believe that the local exchange market would respond differently. In lieu of balloting, therefore, the Company suggests that a combination of a neutral education program and CLECs' own marketing efforts will be sufficient to ensure that customers know they have choices. The Company also supports a customer information center that would serve as a neutral point of contact for customers as well as objective letters sent to all customers by a third party to inform customers of their choices. Company Brief, pp. 49-51.

5. Cost Accounting Manual

The Company argues that the Telco's Cost Allocation Manual (CAM) and the current regulatory environment provide sufficient protection against cross-subsidization even upon reorganization. The Company states that following the reorganization, the Telco will continue to be subject to §§251 and 252 of the 1996 Federal Act, applicable antitrust laws prohibiting predatory pricing and other anti-competitive conduct, the accounting rules set forth in 47 C.F.R. Parts 32 and 64 and the CAM. The Company claims that this body of regulation provides detailed requirements regarding the allocation of costs between regulated and non regulated affiliates. The Company asserts that these safeguards are appropriate to ensure that the Telco is not permitted to improperly shift costs among itself, SAI and its other unregulated affiliates.

The Company also asserts that any redesignation on the corporate books of retail assets to SAI from the Telco should be accounted for at net book value. The Company argues that the proposed reorganization is not a "transaction" within the meaning of the CAM, but is a corporate reorganization caused by major industry and regulatory changes. Consequently, the Telco's CAM is not applicable in this situation because the affiliate transaction rules do not apply. According to the Company, those rules were designed to apply only to routine and ongoing transfers of goods and services that might result in systematic cross-subsidization of a non-regulated affiliate by the regulated entity.

Lastly, the Company contends that given the increasingly competitive nature of the telecommunications market in Connecticut and the proposed corporate reorganization, Holding Company and Telco restrictions and reporting requirements imposed by the Department over the past several years are no longer necessary. The Company argues that subsequent to the corporate reorganization, these restrictions and reporting requirements should be eliminated. Company Brief, pp. 51-55.

B. Office of Consumer Counsel (OCC)

1. Reorganization Proposal

OCC states that the Company's proposal is truly a creative approach to overturning certain requirements in state and federal law and ignores existing channels through which SNET should seek relief from problems it has discussed in this proceeding. OCC cites as an example the 1996 Federal Act's inclusion of the "two percent rule" to provide suspensions or modifications of requirements imposed on local exchange carriers of SNET's size. 47 U.S.C. § 251(f)(2). OCC also notes that Connecticut law permits telephone companies to follow certain procedures to reclassify a service to a less regulated designation if market conditions for that service merit such a reclassification.

OCC contends that SNET's assertion that its proposal will benefit competition does not stand up in the context of the Connecticut and federal laws. OCC states that recent federal and state policy developments make the transition from monopoly telecommunications markets to competitive markets by weakening the market power of the monopoly service provider and not shifting that power to different parts of its corporate structure. OCC claims that a primary purpose of both the 1996 Federal Act and Public Act 94-83 is to relieve the Company of its monopoly, requiring it to lose a portion of its market share and related revenues. OCC asserts that it has no interest in imposing any regulatory restrictions on the Company for its own sake; rather, its interest is in ensuring that federal and state law is adhered to and that competition thrives in Connecticut for the benefit of telecommunications consumers. According to OCC, until effective local service competition emerges in Connecticut, particularly for residential consumers, the consumer's interest will only be protected by continuing Departmental regulation of SNET. OCC contends that the Company's proposal would defeat that interest. Accordingly, as a matter of both state and federal law as well as sound public policy, OCC recommends the Department reject SNET's reorganization proposal. OCC Brief, pp. 5-7; OCC Reply Brief, pp. 5.

2. Successor of an ILEC

Noting the Company's proposal to transfer its retail operations to SAI and no longer offer retail local exchange service from the Telco, OCC maintains that Congress foresaw and prohibited this sort of corporate shuffle to avoid the central requirements of the 1996 Federal Act when it included in the definition of ILEC any "successor or assign" of an ILEC. OCC contends that the monopoly power which Congress was trying to break is not innate to the particular corporate entity of the original ILEC but rather it resides in the services, functions, and facilities of the ILEC, all of which can be transferred to another corporate entity through succession or assignment. According to OCC, as a "successor or assign" of the Telco, SAI is itself an ILEC with respect to its retail service. OCC concludes that treating SAI as a CLEC without the ILEC obligations would thus be a violation of the 1996 Federal Act.

OCC further contends that by imposing greater restrictions on ILECs than CLECs in the 1996 Federal Act, Congress created a disparate regulatory treatment for carriers providing similar services. OCC states that it is clear that Congress wanted

ILECs to be forced to give up some of their monopoly power. In OCC's view, any attempt by the Company to subvert that intention is not legally defensible.

OCC is not persuaded by the Company's argument that SAI would be a CLEC, freed from the additional regulatory obligations imposed on ILECs under the 1996 Federal Act. OCC maintains that as a successor of the Telco SAI would be included in the definition of an ILEC and that the Company misinterprets the plain meaning of the terms "successor" and "assign" as well as FCC guidance on this issue. According to OCC, there is no question that these definitions describe the role that SAI is playing for the Telco under the Company's proposal. OCC contends that SAI is following the Telco into possession by inheritance or succession and that those inherited possessions include, among other things, the Telco's customer base, equipment, employees, reputation as a local telephone company and the strength of its brand.

OCC states that in evaluating the legality of the Company's proposal it is important to remember that the question before the Department is not whether the Telco may transfer its local exchange service to an affiliate. Rather, the issue is whether that affiliate may provide local exchange service and still be considered a CLEC while freeing the Telco from the resale pricing provision of §251(c)(4) of the 1996 Federal Act.

OCC also disagrees with SNET's contention that under the recent Non-Accounting Safeguards Order, SAI would not be treated as an assign of the Telco. According to OCC, the Non-Accounting Safeguards Order explicitly prohibits a BOC from transferring local exchange and exchange facilities and capabilities to "... another affiliate," in order to evade regulatory requirements. Non-Accounting Safeguards Order, ¶ 18. OCC states that the FCC disapproves of efforts by "one service provider to game regulatory requirements." Id. at ¶ 19. Additionally, OCC contends that the very fact that the 1996 Federal Act includes a services-based ILEC resale requirement alongside other, facilities-based requirements indicates Congress' recognition that wholesale access to an ILEC's services is essential to eliminating ILEC monopolies and to enabling new market entrants to compete. OCC claims that there is no indication that Congress saw the resale pricing requirement as somehow less important than the other provisions of §251(c) of the 1996 Federal Act. In OCC's view, it is hard to imagine that Congress intended to limit its definition of a "successor or assign" only to an entity that is the beneficiary of a transfer of facilities to the exclusion of services.

Further, OCC notes that in the Non-Accounting Safeguards Order, the BOCs, argued for a narrow definition of "successor or assign," proposing that an "affiliate could only be a successor or assign if it 'substantially take[s] the place of the BOC in the operation of one of the BOC's core businesses." Non-Accounting Safeguards Order at ¶ 303. Although the Department is not required to define the outer limits of the successor definition in this docket, OCC recommends that the Department adopt a definition at least as broad as the "core business" definition which the BOCs proposed in that FCC proceeding, and determine that the Company's retail local exchange business is a core business.

OCC maintains that a literal reading of §251(h)(1) of the 1996 Federal Act punctuation and clause designations requires that SAI be considered an ILEC if it had been offering local exchange service on the date of the 1996 Federal Act's enactment. However, OCC explains that such a literal reading of that subsection would do damage to the intent of the 1996 Federal Act and would render other provisions meaningless. OCC suggests that the Department include as part of its definition of an ILEC, a "successor or assign" of a carrier that meets both subparagraph (A) and clause (B)(i) of §251(h)(1) of the 1996 Federal Act.

Further, OCC contends that a literal reading of that section of the 1996 Federal Act would permit the Telco to transfer all of its assets, including its network to SAI, while essentially freeing SAI from the ILEC obligations imposed upon the Telco by the 1996 Federal Act. OCC argues that there would be no real difference between the Telco and SAI after the transfer except for a different name. According to OCC, given the ease with which ILECs could evade the explicit provisions of §251(c) of the 1996 Federal Act, (i.e., requirements that ILECs negotiate, interconnect, provide unbundled access, resell retail services at wholesale prices, provide notice of changes, and provide collocation) such requirements would become meaningless.

Additionally, OCC argues that a literal reading of §251(h)(1) of the 1996 Federal Act would run counter to Congress' intent in passing the legislation. OCC states that Congress intended to break the monopoly power of the ILECs by imposing additional obligations on them and not preserving the old monopolies in different corporate shells under new names. Specifically, any RBOC could establish a new affiliate (which did not meet the requirement of §251(h)(1)(A) of the 1996 Federal Act of providing local exchange service as of the date of its enactment), transfer part or all of its assets to the new affiliate, and continue its monopoly over the local exchange market in a particular area without complying with the ILEC requirements. OCC notes that the FCC has previously foreclosed this possibility by not permitting BOCs to transfer local exchange and exchange facilities and capabilities to another affiliate in order to evade regulatory requirements. Therefore, OCC recommends the Department interpret §251(h)(1) of the 1996 Federal Act consistent with the FCC's guidance. OCC Brief, pp. 8-18; OCC Reply Brief, pp. 15 and 16.

OCC further claims that the Public Act establishes a statutory framework and procedures that decrease the level of regulation accorded to increasingly competitive services. OCC states that the only reason SNET eschews the established reclassification procedure is that adhering to such procedures is too heavy a burden and the outcome is too uncertain. OCC argues that neither SNET's convenience nor its desire for a pre-ordained outcome is adequate justification for evading important proceedings and procedures established by the Department and by the Act. OCC maintains that an examination of SNET's market power suggests that the local exchange service market in Connecticut is not competitive and is not ready for the less rigorous regulatory treatment that accompanies a competitive classification.

Moreover, OCC asserts that the Company possesses virtually 100% of the market coupled with the enormous power of incumbency. OCC, while acknowledging the number of certified CLECs, contends that the presence of these service providers will not ensure proper price protection to retail end users. OCC maintains that no amount of economic theory can alter the fundamental fact that the Company retains monopoly power in the provision of local exchange service in Connecticut, particularly for residential and small business consumers. OCC also disagrees with the Company that Connecticut's present retail markets are as close to perfectly contestable as conceivable and SAI would have little or no market power. According to OCC, the fatal weakness of the theory of contestable markets is that it does not apply in the real world. OCC Brief, pp. 22-26.

3. Customer Marketing

In response to the Company's proposed information campaign, OCC believes that there is merit to a proposal to disseminate information to the ratepayers of Connecticut concerning the ramifications of the implementation of the Public Act as well as the 1996 Federal Act. OCC does not believe, however, that it is practical to fund and staff an "answer center" or "information booth" structure since either would be cumbersome and probably lead to improvident sales opportunities. OCC also notes that there is no interest on the part of the Company's competitors to participate in a program in which independent salespeople would be answering customer questions on behalf of all service providers.

As an alternative to the Company's proposal, OCC suggests that an information package be drafted by a committee of the Department, OCC, and other parties to this proceeding and made available to affected customers. OCC states that while there is plenty of information being disseminated in the media, state regulatory bodies could best orchestrate an impartial and informative brochure or letter with basic "how to" customer information. OCC suggests that developed materials be disseminated as information provided by the Office of Consumer Counsel pursuant to an order from the Department. OCC Brief, pp. 28 and 29.

4 Affiliate Transactions

OCC argues that affiliate transactions contemplated by the Company's proposal place customers at risk because the inadequacy or inapplicability of affiliate transaction rules will allow the Telco to discriminate in favor of SAI. OCC disagrees with the Company that the proposed transfer of assets to SAI are not a "transaction" for purposes of its Cost Allocation Manual. According to OCC, in those cases where SAI will compensate the Telco for assets, compensation is set at "net book value" instead of market value. OCC is of the view that other market participants must obtain these same assets at market value if they are to challenge SAI's market position.

OCC also contends that a single affiliate transaction, the transfer of the Telco's customer base, would provide SAI with one of the greatest advantages it would receive under the proposal,. OCC contends that by allowing SAI to receive the entire customer base at no cost, the Department would severely disadvantage other participants who would have to incur significant costs to make inroads into the local market. According to OCC, under this scenario, competition would be impeded and consumer protection would be withheld.

Lastly, OCC claims that the purpose of examining the affiliate transactions is to ensure that there is no cross-subsidization between services performed by the company for any of the competitive affiliates. Tr. 4/3/97, p. 605. OCC argues that SNET's proposal would result in exactly that type of cross-subsidization. OCC asserts that competition would be impeded because SAI would receive through its affiliation with the Telco a lower cost of capital than if it had to obtain funding on its own, as other market participants will. OCC Brief, pp. 28-31.

C. AT&T COMMUNICATIONS OF NEW ENGLAND (AT&T)

1. 1996 Federal Act

AT&T contends that the Company's proposal is patently illegal and a violation of §§251 and 252 of the 1996 Federal Act and inconsistent with the reasoning and intent of §272 of that act. AT&T states that the Company is an ILEC as defined by the 1996 Federal Act and is subject, regardless of corporate structure, to all the obligations of an ILEC. AT&T claims that the Company as currently structured and primarily through the proposed SAI and Telco entities clearly meets the requirements set forth in §251(h)(1)(A) and (B) of the 1996 Federal Act and will retain the obligations of an ILEC under the 1996 Federal Act. AT&T Brief, p. 5.

AT&T argues that §251(h)(2) of the 1996 Federal Act makes explicit the intention that responsibilities of an ILEC never go away. AT&T asserts that while in the future the Company may be composed of many subsidiaries and may transfer functions, assets and employees between or among these subsidiaries, there must always be an ILEC to fulfill all of the ILEC responsibilities of the 1996 Federal Act. According to AT&T, until another carrier has been designated by the FCC as having replaced the Telco as the ILEC, then the Telco retains the responsibilities of an ILEC. AT&T contends that there is no other carrier capable of fulfilling these functions within SNET's territory, nor has the FCC named another carrier. The Company is therefore required to fulfill all of the ILEC responsibilities.

AT&T also argues that the 1996 Federal Act is explicit as to the circumstances under which an ILEC may be exempted from specified requirements. AT&T maintains that the 1996 Federal Act does not provide for the restructuring of the corporate entity in the manner proposed by the Company or it would exempt the Company from its ILEC responsibilities. AT&T also maintains that the Company is not (as suggested by SNET) divesting itself of its retail or wholesale operations; rather, it is providing retail services to end users and wholesale services to CLECs.

Additionally, AT&T contends that the FCC has specifically addressed the separate affiliate issue as it relates to the BOCs and this reasoning is as true for the Company as it is for an RBOC. In AT&T's view, it is apparent from §272 of the 1996 Federal Act that local exchange carriers may not circumvent their resale obligations by restructuring themselves into different arm's-length subsidiaries. According to AT&T, § 272 of the 1996 Federal Act requires RBOCs in certain circumstances, such as the provision of out-of-region interstate services, to establish arm's-length subsidiaries that are separate from any "operating entity" subject to the resale requirements in §251(c) of the 1996 Federal Act. AT&T notes that although §272 of the 1996 Federal Act specifically permits and requires RBOCs to establish arm's-length subsidiaries to provide certain services, it also requires that a separate "operating entity" be maintained to fulfill the carrier's resale obligation.

AT&T maintains that the intent of the 1996 Federal Act is to ensure that the RBOCs could not accomplish through a separate subsidiary what they were prohibited from doing as an ILEC (i.e., combining monopoly operations with competitive long distance service and leveraging their bottleneck). While noting that §272 of the 1996 Federal Act does not directly apply to the Company because it is not an RBOC, AT&T maintains that the Company must not be permitted to leverage its ownership of bottleneck facilities and should be held to its resale obligation, as are RBOCs, irrespective of whether it creates separate wholesale and retail subsidiaries.

AT&T concludes that restructuring in and of itself does not relieve the Company of or allow it to otherwise narrow its ILEC responsibilities under the 1996 Federal Act. AT&T suggests that if the Company's proposed restructure could produce such a result, then all ILECs could similarly restructure themselves to circumvent their ILEC responsibilities under the 1996 Federal Act. AT&T claims that the Company's interpretation of the 1996 Federal Act would render the concept of an ILEC meaningless. AT&T Brief, pp. 6-11.

2. Retail and Wholesale Service Pricing

Additionally, AT&T argues that nowhere does the 1996 Federal Act permit ILECs to "freeze" their retail offerings at a given point in time, so that the ILEC no longer has to offer its retail services for resale. AT&T states that ILEC resale obligations are clear with respect to retail services, including the requirement that they make available any retail telecommunications service that it provides to end users for resale at wholesale discounts. AT&T states that the Company is not divesting itself of its retail operations but is merely establishing separate wholesale and retail subsidiaries. AT&T argues that the Company is continuing to provide retail services, albeit through a subsidiary, and under the 1996 Federal Act must make such telecommunications services available for resale.

AT&T also contends that the Company's proposal to price new wholesale services at cost plus contribution rather than at a wholesale discount, is contrary to the pro competitive resale requirements of both the 1996 Federal Act and the FCC Order. AT&T argues that all of SAI's retail services must be offered for resale at the retail rate, minus avoided costs. According to AT&T, the Company, through the Telco or otherwise, must offer its retail services for resale at a wholesale discount irrespective of the fact that it offers those retail services through a separate arm's-length subsidiary.

AT&T suggests that if SAI were excused from its resale obligations, SAI could begin to change the prices, terms and conditions of its retail services, filing them as new services not available for resale. In AT&T's view, by use of such a loophole, SAI could create a whole new class of retail services and price these services lower than those that would be available for resale at a wholesale discount. AT&T maintains that this is in violation of the resale obligations of the federal law, has dangerous implications on the competitive viability of current CLECs and the potential to chill any new entry by CLECs.

AT&T states that ILEC obligations to resell, unbundle and interconnect are the tri-part cornerstone of Congress' effort to pry open the local marketplace to competition. According to AT&T, the fact that the Telco will offer new wholesale services at TSLRIC plus contribution does not satisfy the requirements of the federal law. AT&T also states that the 1996 Federal Act explicitly states that any telecommunications service offered at retail must be made available at a wholesale discount. AT&T argues that offering new wholesale services at TSLRIC plus contribution simply does not fulfill the Company's resale obligation. AT&T Brief, pp. 11-15; AT&T Reply Brief, pp. 6-13.

3. Service Reclassification

AT&T further argues that Public Act 94-83 prescribes procedures and requirements to reclassify a service as a competitive service. AT&T contends that the Company's proposal does not meet these procedures or requirements and would allow it to avoid the requirements of the Department's price cap regime. Accordingly, AT&T asserts that the Company's proposal must be rejected.

AT&T argues that as a matter of law, the Department lacks authority to reclassify SAI services as competitive in the manner proposed by the Company. According to AT&T, the Act classified only a very few of the Company's services as competitive, while the majority of its regulated services remain in the non-competitive category. AT&T states that the Act also established procedures whereby the Company could petition the Department to change the classification of a service. The Company's restructuring plan ignores these requirements and assumes that all retail services provided by SAI would be competitive. AT&T maintains that the Company should be required to fully comply with the requirements of the Act and the Department's reclassification procedures before any of its services can be reclassified, irrespective of whether they are provided by the Telco, SAI or any other subsidiary.

Additionally, AT&T disagrees with the Company's claim that once SAI's application for a CPCN is approved all services provided by SAI as a CLEC "will be deemed 'competitive' telecommunications services." AT&T argues that the issue before the Department is not whether services provided by a CLEC are competitive by virtue of being provided by the CLEC. Rather, the issue is whether, under the Act, the Department must: (1) follow the procedures established for determining the classification (i.e., non-competitive, emerging-competitive, competitive) of each of the individual services the Company proposes to transfer to SAI; (2) determine in accordance with this procedure that each of the services to be transferred is competitive; and (3) do so before it approves the transfer of any service it finds to be competitive to SAI, to the extent it approves SAI's application as a CLEC.

Regarding the Company's proposal that the Department reclassify its services as competitive based upon the criteria contained in Conn. Gen. Stat. §16-247(f)(d), AT&T contends that the Company's presentation is inadequate. According to AT&T, a mass reclassification of the Company's retail services, under any circumstances, is clearly inappropriate. AT&T states that the express language of the statute, as well as the legislative history and intent of the Act, envisioned a service-by-service reclassification procedure wherein the Department would consider eight criteria before deciding whether to reclassify a service. AT&T also states that the instant docket was not established to reclassify services nor did the parties have an opportunity to evaluate and respond to the Company's alleged proffer of proof. AT&T suggests that if the Company wishes to reclassify its services it should do so in the context of a docket where such issue is expressly presented.

AT&T states that in addition to circumventing its obligations under the Act, the Company is seeking to remove itself from price cap regulation as established by the Department in its March 13, 1996 Decision in Docket No. 95-03-01. AT&T claims that under the Company's reorganization proposal, retail prices will be no longer subject to any price ceiling, even if the services were not yet competitive and the ratepayers would receive no protection whatsoever. According to AT&T, the Company's proposal to escape obligations imposed on it by the alternative regulation plan violates Public Act 94-83 and the Decision in Docket No. 95-03-01. AT&T therefore suggests that the Company's proposal be rejected. AT&T Brief, pp. 16-22; AT&T Reply Brief, pp. 14 and 15.

4. Arbitrated Awards

AT&T also argues that the Company's proposal to resell only those retail services that exist in its retail tariff as of the effective date of any allowed restructure and to price all new wholesale offerings at cost plus contribution violates the AT&T/SNET arbitration award and must be rejected. AT&T maintains that as part of the Department-approved Arbitration Award between AT&T and SNET in Docket No. 96-08-08, Application of AT&T Communications of New England, Inc. for Arbitration with the Southern New England Telephone Company Under the Telecommunications Act of 1996, the parties agreed that:

> SNET shall tariff and make available to AT&T, at wholesale rates, all of SNET's retail telecommunications services on the same terms and conditions contained in the retail tariffs for those services, except as otherwise specifically set forth in this Agreement. [11]

AT&T claims that at no time during these negotiations did SNET indicate its intention to limit the availability of retail services in the manner or time frame as

[11] Docket No. 96-08-08, Decision, dated December 4, 1996, p. 12.

proposed in the instant proceeding. AT&T contends that the Company should not be permitted to change the agreement the Company entered into before it filed its January 24, 1997, restructuring proposal. AT&T asserts that the Department has established that the arbitration awards should take precedence over any generically established rates. Therefore, the Company should not be permitted to change rates specifically awarded as part of the arbitrations, especially those rates which were negotiated and agreed to for a specified period of time. AT&T Brief, pp. 22-25

5. Market Contestability

AT&T states that the level of deregulation sought by the Company is not commensurate with the level of competition present in the local exchange service marketplace and is unnecessary in light of the current regulatory framework in Connecticut. AT&T claims that the Company's proposed restructuring will unleash the incentives and opportunities dominant monopoly providers of services have at their disposal to discriminate against potential rivals. According to AT&T, these incentives and opportunities would present significant hazards to the continued development and growth of local exchange competition in Connecticut.

AT&T also disagrees with the Company's claim that the local exchange market in Connecticut is contestable because the 1996 Federal Act has put in place provisions designed to remove barriers to competitive entry. AT&T states that the Company's reliance on these provisions to demonstrate the contestability of the market allows the Company to ignore the fact that these are the same provisions it (the Company) admits it seeks to circumvent by its proposed restructure. Further, AT&T disagrees with the Company's claim that in order to determine contestability, the market to be analyzed is the totality of the local, intrastate and interstate toll markets. AT&T argues that the appropriate market is the local exchange marketplace and would not be contestable if: (1) the wholesale portion of the firm (Telco) finds subtle but effective ways to discriminate in favor of its retail subsidiary (SAI) and (2) new entrants must incur considerable sunk costs to enter the local market.

In AT&T's view, circumstances which prevent a market from being contestable are exactly those which exist in the present Connecticut local exchange service market. AT&T asserts that if SNET's proposal is approved, the Telco will have many opportunities to discriminate in favor of SAI. For example, the Telco and SAI possess an ability to share pre-existing billing and electronic ordering, provisioning, maintenance and repair arrangements, while new entrants will be required to develop, deploy and pay for such arrangements with the Telco. AT&T posits that the Telco could slow down or hinder the development of such interfaces with new entrants, while maintaining and strengthening the built-in advantage SAI enjoys by virtue of its pre-existing interfaces.

While SAI has reserved the right to negotiate and sign separate interconnection agreements with the Telco, AT&T claims that no new entrant can expect to negotiate term and volume discount arrangements as attractive as those to be made available by the Telco to SAI. AT&T asserts that no new CLEC could hope to penetrate the local marketplace because SAI will be able to offer lower prices than its competitors because of SAI's pre-existing relationships with the incumbent.

Finally, AT&T maintains that the Company's attempt to circumvent the Act's specific imputation standard presents it with another opportunity to discriminate against CLECs by placing them in a price squeeze hindering local market entry. AT&T asserts that the Company wishes to eviscerate the imputation standard by agreeing to an aggregate imputation standard. According to AT&T, an aggregate imputation standard allows the Company to demonstrate that over a broad spectrum of services its prices in total or in aggregate are greater than the corresponding wholesale prices charged to competitors. AT&T states that this would allow the Company to maintain high prices for some services (e.g., toll), while placing its competitors in a price squeeze for local services. AT&T contends that an effective service-by-service imputation standard must be in place.

Additionally, AT&T argues that the theory of contestable markets assumes entrants do not have sunk costs. AT&T states that this is not the case in the Connecticut local exchange market because resellers and facilities-based carriers have sunk costs of entry, although the level of sunk costs for resellers may be lower. AT&T cites as an example the marketing costs of getting customers to switch their carriers. AT&T also claims that new entrants must expend substantial time and costs in developing billing systems and electronic interfaces with the Company for ordering, provisioning, maintenance and repair, etc., expenses which SAI will not experience. AT&T also claims that the development and deployment of these systems have been a major hurdle for it to enter the local market on a ubiquitous basis and in conformance with the quality of service expected by today's customers.

Furthermore, AT&T contends that only when sufficient alternatives exist to the Company's resale services and unbundled network elements, will competitive local exchange carriers be freed from the Company's monopoly grip and be able to shop elsewhere for these services. AT&T states that only when facilities-based competition truly develops will CLECs have the ability to purchase resale or unbundled network elements from other sources. Until then, the Company's reorganization proposal is seriously premature, because discriminatory behavior by it or its subsidiaries, or failure to enforce an effective imputation standard will hinder competition in the local market.

AT&T disagrees with the Company's suggestion that the relevant market that should be examined in order to determine whether the level of competition justifies the extensive deregulation sought by the Company is the combined local, intraLATA toll and interstate market. AT&T asserts that examining these very distinct markets in aggregate will serve to obfuscate the level of competition present in each especially the local marketplace. Noting that the Company has admitted to retaining over 99% of all local customers, AT&T states that it is ridiculous to argue that an ILEC who owns the local bottleneck network and maintains more than a 99% market share should be granted the type of price deregulation for its local services sought by the Company. AT&T also states that the Company has been providing intraLATA toll service as the incumbent LEC for over 100 years while other carriers were not permitted into this market until 1988, and could not effectively compete until intraLATA presubscription was fully deployed at the end of 1996. AT&T maintains that the Company has an enormous advantage in the intraLATA toll market place due to its ability to leverage its position as the local service provider for more than 99% of Connecticut's customers. SNET, by virtue of reclassifying its intraLATA toll service as a competitive service, has all the pricing flexibility it needs to compete in this market.

AT&T contends that SNET has been very successful in the interstate toll marketplace gaining more than 30% of the market share. SNET is not required to resell its interstate toll services at a wholesale discount and, therefore, is not disadvantaged in this market by its resale obligation imposed by federal law. AT&T concludes that the Company's resale obligation has not resulted in any appreciable erosion of its monopoly hold over the local market. Additionally, the Company's resale obligation does not materially affect the dynamics of the intraLATA market where its largest competitors do not resell its services or the interstate market where it is very successful and is not obligated to resell its services at a wholesale discount. AT&T Brief, pp. 26-34.

6. ILEC Obligations

AT&T argues that the reason the 1996 Federal Act and FCC place resale, unbundling and interconnection obligations on an ILEC is to open the monopoly hold they have on the local exchange market. AT&T disagrees with the Company's contention that the 1996 Federal Act and FCC's implementing orders place onerous asymmetric regulation on an ILEC such that it will be unable to compete against CLECs in terms of price, product innovation or service. According to AT&T, the Company continues to retain its competitive advantage by virtue of the fact that it has the vast majority of local customers in the state, owns the existing bottleneck local network, is not burdened with the enormous costs of initial local market entry as are CLECs, and has been extremely successful in the long distance market. AT&T states that the Company's claim that it is at a competitive disadvantage to new entrants trying to break into the local market strains credulity.

AT&T also disagrees with the Company's argument that the Telco's obligation to offer for resale new innovative service packages prevents it from effectively competing with new entrants. AT&T claims that the Company's argument is flawed in two fundamental respects. First, the historical development of competition in the interstate marketplace has shown that resale of long distance services has not hindered innovation and competition. Citing its own experience in the interstate market, AT&T states that it has not been precluded from offering innovative, long distance services, and notes that the long distance marketplace is now characterized by an abundance of innovative competitive offers, (e.g., SNET's All Distance, MCI Friends and Family, and Sprint 10¢ A Minute). Additionally, AT&T states that of the six services which the Company claims will be included in service packages that will be increasingly prevalent in a competitive marketplace (i.e., local service, interstate and intrastate toll, video, wireless and on line services), only two must be made available for resale at wholesale discounts under the 1996 Federal Act and FCC Order whether included in a package or not, (i.e., local and intrastate toll services). AT&T states that the other four services are not required to be made available for resale at wholesale discounts. AT&T notes that the Company's largest CLEC competitors provide intrastate toll services over their own networks and it is unlikely that they would seek to resell these services from the Telco.

AT&T also disagrees with the Company's claims that it (the Company) is at a competitive disadvantage when reselling promotional offerings of greater than 90 days. AT&T asserts that the Company ignores the fact that for promotions of 90 days or less, it has a competitive advantage over CLECs because ILECs are not required to resell such promotions at a wholesale discount. According to AT&T, the FCC has struck a balance between the benefits of short term promotions and the potential for abuse of long term promotions by limiting the ILEC's resale obligation to promotions exceeding 90 days. AT&T argues that the Company should not be permitted to circumvent its resale requirements with respect to such promotions by creating an arm's-length subsidiary.

Regarding the Company's claim that its ability to differentiate its retail services from those offered by CLECs is limited because it is required by law to resell those same retail services , AT&T states that the Company ignores the fact that it is an ILEC who owns the bottleneck and local network. AT&T claims that this is precisely the reason new entrants must purchase wholesale services and unbundled elements from an ILEC at a discount in order to enter the local market on a widespread basis. AT&T maintains that the requirement that the service an ILEC provides to CLECs must be at parity to the service it provides to itself and to its customers is necessary because an ILEC could hinder local market entry if it were permitted to offer wholesale services and unbundled network elements to new entrants at less than parity. AT&T contends that the inability to purchase services from an ILEC at parity with the quality offered in the ILEC's retail services tilts the competitive playing field to the ILECs.

AT&T asserts that the Company's reorganization proposal will do nothing to remedy the Company's perceived disadvantage in the market. AT&T states that since SAI will resell the Telco's services and will be subject to the same general prices, terms and conditions as any other CLEC, SAI's retail services will always be at quality parity with any other CLEC who purchases services from the Telco. AT&T further states that even if SAI paid a premium to the Telco for better service quality for certain services, any other CLEC could presumably pay the same premium and purchase the same quality of service. AT&T concludes that the Company's argument that its service parity obligations vis-à-vis its retail and CLEC customers places it at a competitive disadvantage and, therefore, justifies its proposed reorganization is without merit. AT&T Brief, pp. 34-45; AT&T Reply Brief, pp. 21 and 22.

7. Level of Regulation

Additionally, AT&T disagrees with the Company's claim that its reorganization plan will leave SAI in exactly the same situation as any other CLEC. AT&T contends that SAI would retain significant advantages over new entrants. For example, unlike any other new entrant, SAI will come into existence with the transfer of all of the telephone company's current residential and business local customers, making it the largest CLEC in Connecticut. Furthermore, AT&T contends that SAI will inherit an established and recognized brand name, operational linkages with its wholesale provider (Telco) and the Directory Publishing units, and an incumbent corporate parent that also owns the monopoly local network and numerous related enterprises which SAI is likely to employ in developing bundled service offerings to its end user customers. AT&T argues that these advantages as the successor of the Company are a significant value that SAI's competitors do not have, and set SAI apart from and in a more favored position than its competitors. Therefore, AT&T concludes that SAI should not be regulated as a CLEC. AT&T Brief, pp. 45-52.

8. Customer Marketing

Regarding the Company's customer notification proposal, AT&T claims that it is unfairly discriminatory. AT&T states that it would be difficult to design a center that is completely competitively neutral, especially when the Company proposes to fund the center. AT&T concludes that the Company's proposal to fund a competitively neutral information center should be rejected. According to AT&T, the proposed information center would provide little, if any benefit, to the average consumer and serve only to confuse most customers. AT&T contends that the only carrier who would benefit from this confusion would be the incumbent. AT&T Brief, pp. 53-55.

9. Company Regulatory Structure

Lastly, AT&T argues that despite the Company's assertions, transferring retail services to SAI, where it will avoid almost all state regulation, is not necessary to allow SNET to compete effectively in the local market. AT&T states that Connecticut anticipated, and planned for, the development of local competition with the passage of Public Act 94-83. AT&T maintains that under the authority of the Act, SNET sought and was allowed a form of alternative regulation. The regulatory structure now in place in Connecticut was carefully designed to facilitate and encourage the development of competition, including the Company as one of the competitors. AT&T asserts that the Company should not now be allowed to restructure and escape regulation over its retail services entirely.

AT&T claims that in further pursuit of the legislative goal to match the level of regulation to the level of competition, the Act encouraged the Department to implement an alternate form of regulation. The Company proposed, and the Department accepted, a plan that provides separate pricing mechanisms for noncompetitive, emerging competitive and competitive services. According to AT&T, the alternative regulation plan gives the Company increasingly greater pricing flexibility as the level of competition increases.

AT&T asserts that it is critical to recognize that there still is not significant local service competition in Connecticut. AT&T comments that SNET has not sought to reclassify local service as other than a noncompetitive service. AT&T also asserts that the proposed reorganization plan is an attempt to avoid the alternative regulation structure entirely with respect to its retail services. AT&T states that the Public Act and the alternative regulation plan approved by the Department in Docket No. 95-03-01, recognizes that a continuing, but decreasing, level of regulation is necessary and appropriate during the transition from a monopoly environment to a truly competitive marketplace. AT&T argues that SNET has not presented any evidence in this docket to change the conclusion reached in Docket No. 95-03-01 that the decreasing level of regulation provided by the alternate regulation plan is the appropriate way to deal with this period of transition. AT&T Brief, 55-59.

D. MCI TELECOMMUNICATIONS CORPORATION (MCI)

1. Reorganization Proposal

MCI states that when viewed in the context of the Connecticut Telecommunications Task Force's work, the new regulatory compact established by the Connecticut Legislature under Public Act 94-83 and the Department's efforts over the past three years to implement the Act, the Company's proposal squarely conflicts with the state telecommunications law and policy as carried out by the Department over the past three years. MCI claims that SNET has ignored the Department's admonition at the outset of this proceeding that "SNET's affiliate strategies, structures and standards conform with the prevailing rules and regulations governing telecommunications providers"[12] and has recommended a proposal that far exceeds the scope of the instant docket.

MCI argues that the Company's proposal fails to comply with the requirements of the Act applicable to the reclassification of telecommunications services. MCI also argues that since SNET has not complied with the service reclassification process and admitted that its proposal is not a request for service reclassifications in accordance with §16-247f of the Conn. Gen. Stat. the Department is without any statutory authority to reclassify SNET's retail services. MCI maintains that SNET can only transfer or assign noncompetitive services to SAI and that SAI cannot acquire as successor to SNET any service classifications other than those held by SNET at the time of such transfer or assignment.

MCI asserts that SNET's proposed plan violates the Decision in Docket No. 95-03-01 that approved an alternative form of regulation for SNET, as well as Conn. Gen. Stat. §16-247k, which authorizes and limits the alternative form of regulation available for adoption by the Department. According to MCI, the alternative form of regulation previously adopted by the Department expressly made the Company's retail services subject to the service reclassification requirements of Conn. Gen. Stat. §16-247f, for the term of the approved plan. MCI contends that the Company's proposal violates service reclassification requirements in that the effect of approval of the proposed plan constitutes a reclassification of all of SNET's telecommunications services to the competitive category without regard to the substantive or procedural requirements of Conn. Gen. Stat. §16-247f or the Department's Decision in Docket No. 95-03-01. MCI

[12] Statement of Scope of Proceeding, p. 2.